No. 87-654

**IN THE SUPREME COURT OF THE UNITED STATES**

**October Term, 1987**

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**NEW ENERGY COMPANY OF INDIANA,**
*Appellant,*

v.

**JOANNE LIMBACH,** *et al.*,
*Appellees.*

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**On Appeal from the Supreme Court of Ohio**

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# MOTION OF APPELLEE SOUTH POINT ETHANOL TO AFFIRM OR DISMISS

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## QUESTION PRESENTED

Whether an Ohio statute violates the Commerce Clause by providing that a special tax incentive to fuel dealers designed to encourage the production and use of ethanol in Ohio and other states is inapplicable to fuel containing ethanol produced in a state that does not provide a similar tax incentive for fuel containing ethanol produced in Ohio, despite the statute's lack of either a protectionist purpose or a detrimental effect on interstate commerce.

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## MOTION OF APPELLEE SOUTH POINT ETHANOL TO AFFIRM OR DISMISS

At issue on this appeal is the validity of Ohio Rev. Code § 5735.145(B), which provides that a special tax incentive to fuel dealers designed to encourage the production and use of ethanol in Ohio and other states is inapplicable to fuel containing ethanol produced in a state that does not provide a similar tax incentive for ethanol produced in Ohio. Appellant New Energy Company of Indiana ("New Energy") has abandoned challenges grounded on the Privileges and Immunities and Equal Protection Clauses of the United States Constitution and appeals only on the theory that Ohio Rev. Code § 5735.145(B) offends the Commerce Clause, U.S. Const. art. I, § 8, cl. 2. The Ohio courts properly rejected this theory, and New Energy has presented this Court with no issue warranting plenary review. Accordingly, the decision of the Supreme Court of Ohio should be summarily affirmed or, in the alternative, the appeal should be dismissed.

## STATEMENT OF THE CASE

Among the many environmental and economic benefits associated with ethanol use, perhaps the most significant is a

reduction in toxic emissions from leaded automobile fuels, which the Environmental Protection Agency has deemed a serious public health problem. 49 Fed. Reg. 31,036 (1984). Lead is toxic to preschool and unborn children and has been linked to high blood pressure in adults. 50 Fed. Reg. 9401 (1985). Gasoline is "the most ubiquitous source of lead emission in the environment." 49 Fed. Reg. at 31,038. Because its octane-enhancing abilities enable it to replace lead in gasoline, ethanol is the most promising motor vehicle fuel additive today. Amended Agreed Findings of Fact ("Finding") 10, South Point App. 3a. Despite assertions to the contrary in its Jurisdictional Statement, New Energy itself has conceded that ethanol is the most cost-effective and environmentally benign replacement for lead in gasoline. *Id.*

Because of the substantial benefits associated with the use of ethanol as a motor vehicle fuel additive, the federal government and many states have initiated programs to make viable its production and use. Findings 10, 11, 13, New Energy Finding 11, South Point App. 3a-4a, 7a. The most effective of these programs have involved tax credits, which have been employed by the federal government and at least thirty-two states to make ethanol production and use possible. Finding 11, New Energy Finding 11, South Point App. 3a, 7a. These incentives are, for all practical purposes, responsible for the present existence of substantial interstate commerce in ethanol. New Energy's chief executive officer testified at trial that, due to the high cost of producing ethanol, absent federal and state incentives "ethanol would not be a viable factor in the market place today." Mar. 1 Hg. 17.[1]

Joining the federal government and many other states, Ohio has recognized the benefits associated with ethanol use and has used tax incentives to subsidize the development and growth of interstate commerce in ethanol. Finding 13, South Point App. 3a-4a. Although it could have chosen (as did New Energy's

1 Evidence from the March 1, 1985 and March 29, 1985 trial court hearings in the case will be referenced as "Mar. 1 Hg. ___" and "Mar. 29 Hg. ___," as in New Energy's Jurisdictional Statement.



state, Indiana) to encourage the in-state production of ethanol by means of a direct subsidy available only to Ohio ethanol producers, Ohio's General Assembly has attached such value to the use of ethanol that it has been willing to indirectly subsidize both in-state and out-of-state ethanol producers.

This appeal arises from the fact that Ohio's willingness to subsidize out-of-state ethanol producers has not been completely unlimited; that willingness has instead been conditioned on the availability in those producers' states of a similar indirect subsidy for Ohio-produced ethanol, a limit which was intended, among other things, to provide an incentive to other states to enact ethanol tax credits and which is fully consistent with the goal of stimulating ethanol production and use on a national basis. New Energy Finding 21, South Point App. 8a.

The Ohio ethanol credit is tied to a fuel tax that Ohio imposes on retail dealers for each gallon of gasoline sold in the state. Ohio Rev. Code §§ 5735.01-5735.99. Under Ohio Rev. Code § 5735.145, fuel dealers are granted a credit toward this tax of 2.5¢ per gallon for the sale of gasoline that is blended with not more than ten percent ethanol. This credit is available for gasoline blended with ethanol ("gasohol") produced in Ohio or in any other state, unless the state of origin does not grant "an exemption, credit or refund from such state's motor vehicle fuel excise tax or sales tax for similar fuel containing ethanol produced in Ohio." Ohio Rev. Code § 5735.145(B).[2]

Ethanol produced in numerous other states is eligible for Ohio's special tax incentive, and an abundance of ethanol produced outside of Ohio is available to Ohio retailers. Finding 17, South Point App. 5a. Of the midwestern states, Ohio, Kentucky, Tennessee, Iowa, Illinois and Minnesota all provide tax incentives for gasohol sales. The only ethanol producer with

2 New Energy states in the Questions Presented section of its Jurisdictional Statement that the Ohio statute denies a credit for ethanol produced out of state unless the producer state grants "at least as high" a credit there for Ohio-produced ethanol. Jurisdictional Statement at ii. This is untrue. The Ohio statute provides a credit for ethanol produced in all states granting a reciprocal tax credit in any amount. Ohio Rev. Code § 5735.145(B).

an Ohio production facility is Appellee South Point Ethanol ("South Point").[3] Out-of-state ethanol producers who sell to Ohio dealers include Archer Daniels Midland ("ADM"), Pekin Energy ("Pekin"), and A.E. Staley ("Staley"). ADM, the largest producer of ethanol in the United States, and Pekin have production facilities in Illinois. Staley has production facilities in Tennessee. Ohio dealers selling gasoline blended with ethanol produced by ADM, Pekin, or Staley in Illinois or Tennessee, as well as with ethanol produced by South Point, are entitled to the Ohio ethanol tax credit. *Id.*

Ethanol produced in Indiana by New Energy, however, does not qualify for the Ohio tax incentive under Ohio Rev. Code § 5735.145(B) because Indiana decided in 1984 to limit its support of ethanol production to ethanol produced in Indiana. In implementing this decision, Indiana eliminated its ethanol tax credit, which was available for ethanol produced in other states as well as in Indiana, and replaced it with a direct subsidy available only to Indiana ethanol producers — the only one of which was New Energy.[4] As a result, ethanol produced by New Energy, which has been directly subsidized by Indiana, no longer qualifies for Ohio's ethanol tax credit, and New Energy's ethanol is thus less attractive to Ohio fuel dealers than ethanol produced in states like Illinois and Tennessee and in Ohio.

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3. South Point is an Ohio partnership. A Sup. Ct. R. 28.1 listing of corporate affiliations is therefore not provided.

4 Before the Fall of 1984 when New Energy began to compete in the ethanol market, Indiana encouraged the use of ethanol by applying a lower tax rate to all retail gasohol sales than the rate for retail gasoline sales. In anticipation of New Energy's entry into the market, however, in March 1984 the Indiana legislature repealed the lower tax rate for ethanol, effective July 1, 1985, and, in the same bill, replaced this lower tax rate with the Ethanol Fuel Production Incentive Grant, which is in effect a production credit available *only* to New Energy. Mar. 1 Hg. 20-22; Mar. 29 Hg. 8-9. Following the trial in this case, Indiana law was amended to retain only 1¢ per gallon of ethanol blend credit. With the combination of the Indiana production grant (1.5¢ per blend gallon) and the Ohio credit (1¢ per blend gallon), New Energy was in fact not at a competitive disadvantage with South Point. These grants have since been discontinued in Indiana.



The trial court found that the unavailability of the Ohio tax credit will cause severe financial hardship to New Energy. Finding 20, New Energy Finding 20, South Point App. 5a, 8a. But Ohio Rev. Code § 5735.145(B) does not preclude New Energy from selling ethanol in Ohio. It merely affects the price New Energy must charge in Ohio for its product in order to compete effectively for Ohio business with other ethanol producers (only one of which is located in Ohio). Finding 18, South Point App. 5a.

To the extent that Ohio's unwillingness to subsidize New Energy's ethanol production makes it uneconomical for New Energy to sell its ethanol in Ohio (a point on which the trial court made no finding but merely stated New Energy's view, *see id.*), no burden is imposed on interstate commerce. Two compelling reasons support this conclusion.

First, New Energy's assertion that it cannot profitably market ethanol in Ohio absent a state tax incentive translates directly into a conclusion that without the tax incentive there would be *no* commerce in ethanol. Mar. 1 Hg. 17. Ohio's tax incentive may not be as broad as New Energy would like, but New Energy's own contention, if true, clearly demonstrates that the Ohio incentive actually *encourages* the flow of interstate commerce. Second, the trial court found that ethanol producers from states other than Ohio, which are eligible for Ohio's tax incentive, could supply the portion of the Ohio ethanol market that New Energy had been supplying before the enactment of Ohio Rev. Code § 5735.145(B). Finding 17, South Point App. 5a. Although Ohio Rev. Code § 5735.145(B) may have the effect of reducing New Energy's market share for ethanol in Ohio, New Energy presented no evidence that the statute was protectionist in its purpose or effect or that it would in any way affect the mix of in-state and out-of-state ethanol sold in Ohio or reduce the flow of ethanol into Ohio from other states.

## ARGUMENT

New Energy's attack on the reciprocity provision of Ohio Rev. Code § 5735.145(B) wholly ignores the manner in which the challenged provision operates and relies instead on a hodge-podge of general principles applied with little or no analysis. Distilled to its essence, that attack rests on no more than the erroneous assumption that reciprocity provisions are invalid per se, regardless of their impact, or lack of impact, on interstate commerce. That assumption cannot withstand scrutiny, and New Energy's proof at trial and arguments on appeal provide no alternative basis for invalidating Ohio Rev. Code § 5735.145(B).

### I. The Statutory Limit On Ohio's Willingness To Subsidize The Growth And Development Of Interstate Commerce In Ethanol Is Fully Consistent With This Court's Reciprocity Decisions.

One of the numerous purposes supporting the enactment of Ohio Rev. Code § 5735.145(B)[5] was to promote domestic industry by influencing other states to enact similar tax incentives to encourage the use of ethanol. New Energy App. 63a (trial court opinion). The Ohio legislature chose to further this purpose by creating a tax incentive to stimulate the development and nationwide expansion of a market that would not otherwise have existed. Mar. 1 Hg. 17. Because the ethanol market owes its existence to incentives such as the Ohio tax credit, this case raises very different issues than did prior cases before this Court which involved reciprocity provisions. The Ohio statute does not, in fact, even implicate Commerce Clause

5 The other purposes include: providing a cleaner and safer environment by reducing the amount of lead in gasoline, providing an outlet for the sale of corn surpluses, creating a savings in federal farm and agricultural programs, boosting rural economies and decreasing U.S. dependence on foreign oil. Findings 1, 10, South Point App. 1a, 3a; Mar. 1 Hg. 8-9, 12-13. In this Motion to Affirm or Dismiss, South Point has focused on the purpose of promoting domestic industry by influencing other states because it is this purpose that New Energy has attacked. Jurisdictional Statement at 13-18.



concerns because, rather than obstructing the natural flow of interstate commerce, the statute actually *creates* an interstate market. It surely should be constitutional for a state to enact such legislation that reflects the very principles the Commerce Clause was enacted to protect.

Although they were decided under the Equal Protection Clause, this Court's recent decisions in *Metropolitan Life Insurance Co. v. Ward*, 470 U.S. 869 (1985), and *Western & Southern Life Insurance Co. v. State Board of Equalization*, 451 U.S. 648 (1981), shed substantial light on this case. Both *Ward* and *Western & Southern* involved discriminatory state taxes imposed on insurance companies, and together they stand for the proposition that promoting the *in-state* business of domestic companies by penalizing foreign companies who also want to do business in the state is not a legitimate state purpose, but that promoting the *interstate* business of domestic companies by deterring other states from enacting discriminatory or excessive taxes is a legitimate state purpose. *Ward*, 470 U.S. at 876-878; *Western & Southern*, 451 U.S. at 671. As the Court noted in *Ward*, whether a state's promotion of local industry is a valid purpose under the Commerce Clause (as opposed to the Equal Protection Clause) depends on whether that purpose implicates local or national interest. 470 U.S. at 876 n. 6.

Ohio's ethanol tax incentive is designed to encourage the use of ethanol in Ohio and thus to spur its production in Ohio and elsewhere. It applies to both foreign and domestic ethanol and is not intended to provide an advantage to Ohio ethanol producers at the expense of foreign ethanol producers who compete for the business of Ohio fuel dealers. The reciprocity limitation on the Ohio tax incentive does not affect the legitimacy of Ohio's objective. That limitation is not intended to increase Ohio producers' share of the Ohio ethanol market, but to encourage other states to provide similar incentives, one effect of which is to enable Ohio producers to market their product in other states.

Here, as California did in *Western & Southern*, Ohio has attempted to influence the policies of other states in order to

promote the production and use of ethanol on a national basis and to "enhance its domestic companies' ability to operate interstate." *Ward*, 470 U.S. at 878. Ohio has not, as Alabama did in *Ward*, "erected barriers to foreign companies who wish to do interstate business in order to improve its domestic [companies'] ability to compete at home." *Id.*

Under the standard established in *Ward* and *Western & Southern*, therefore, the objectives underlying Ohio Rev. Code § 5735.145(B) are perfectly legitimate.[6] The manner in which Ohio has pursued its objective of promoting the production and use of ethanol is equally legitimate.

New Energy speaks in sweeping and general terms of Ohio's "discrimination" against businesses from another state, but never identifies any barrier to interstate commerce created by Ohio Rev. Code § 5735.145(B). The reason for this absence of proof is clear: the challenged statute imposes no such barrier and does not prevent or impede the movement of ethanol in interstate commerce. The premise of New Energy's argument on this appeal is not that Ohio has created some *artificial barrier* to interstate commerce in ethanol, but rather that the Commerce

6 Appellant attacks the legitimacy of Ohio's purpose of encouraging other states to enact similar ethanol tax credits, citing *Baldwin v. G.A.F. Seelig, Inc.*, 294 U.S. 511 (1935) and *Brown-Forman Distillers Corp. v. New York State Liquor Authority*, 476 U.S. 573 (1986). Ohio has only attempted to *encourage* other states, however, not to regulate outside its borders as was the case in *Baldwin* and *Brown-Forman*. In *Baldwin*, the New York legislature prohibited in-state sales of milk bought outside of New York unless the price paid to the out-of-state producer was no lower than the minimum price payable to New York producers. This Court held that New York's indirect regulation of prices paid in other states to producers located there unduly burdened interstate commerce. *Baldwin*, 294 U.S. at 524. Similarly, in *Brown-Forman* a New York law prohibited the wholesale sale of liquor at prices any higher than the lowest price that seller would charge for its product elsewhere in the United States during the same month. The Court held that this attempt to "'project its legislation into [other States] by regulating the price to be paid' for liquor in those States" violated the Commerce Clause. *Brown-Forman*, 106 S. Ct. 2080, 2086 *(quoting Baldwin*, 294 U.S. at 521). Attempting to influence other states, without attempting to actually legislate extraterritorially as New York did in *Baldwin* and *Brown-Forman*, is an entirely legitimate state purpose. *Western & Southern*, 451 U.S. at 671.



Clause has been violated because the *artificial incentive* to such commerce embodied in Ohio's ethanol tax credit has not been extended to ethanol produced by New Energy.

The federal government and many states have recognized the benefits of using ethanol as a motor vehicle fuel additive. Finding 11, New Energy Finding 11, South Point App. 3a, 7a. Many of those benefits, however, are noneconomic in nature. The development of interstate commerce in ethanol has thus required an extensive governmental commitment. In Ohio, as in many other states, that commitment has taken the form of a tax incentive to users of ethanol. New Energy's chief executive officer testified that the company would be unable profitably to market ethanol in Ohio absent the tax credit because the price that New Energy would receive would be too low in relation to its production costs. Mar. 1 Hg. 17. In other words, without the Ohio tax credit there would be no market for, or commerce in, ethanol in Ohio, no matter where the ethanol was produced. As a result, this case cannot be characterized as one in which "the State interfered with the natural functioning of the interstate market either through prohibition or through burdensome regulation." *Hughes v. Alexandria Scrap Corp.*, 426 U.S. 794, 806 (1976).

This fact clearly distinguishes the reciprocity decisions on which New Energy relies. In *Great Atlantic and Pacific Tea Co. v. Cottrell*, 424 U.S. 366 (1976) *("A & P")*, for example, Mississippi banned the sale of all milk from other states unless the producer state accepted Grade A milk from Mississippi. In striking down this reciprocity clause, the Court found that it had a "devastating effect upon the free flow of interstate milk," *id.* at 375, and did not serve any legitimate interest of the state. Similarly, in *Sporhase v. Nebraska ex rel. Douglas*, 458 U.S. 941 (1982), Nebraska banned the withdrawal of ground water intended for use in any adjoining state unless that state granted reciprocal rights for the use of its water in Nebraska. This reciprocity provision, which did not significantly advance any legitimate state interest, *id.* at 958, "operate[d] as an explicit barrier to commerce between" Nebraska and Colorado, *id.* at

957, and prevented commerce in water that otherwise would have occurred.

This case presents facts far different from those in *A & P* and *Sporhase*.[7] In each of those cases, the challenged reciprocity provision burdened interstate commerce by preventing or drastically reducing the flow of goods across state lines. The same cannot be said here, in light of New Energy's admission that there would be no commerce in ethanol in Ohio absent the Ohio tax incentive. Because it provides a tax incentive to all out-of-state ethanol except ethanol from states lacking similar incentives, the Ohio statute is a narrowly tailored means to encourage free trade among the states. The statute invites cooperation, not retaliation, from other states. Invalidation of Ohio Rev. Code § 5735.145(B) would require a conclusion that the Commerce Clause prohibits a state that has decided to use its tax laws to make economically viable a product for which there would otherwise be no market from structuring its tax incentive in such a way as to encourage other states to provide similar incentives. Commerce Clause jurisprudence simply does not support this result.

On that score, the instant case bears a strong resemblance to *Hughes v. Alexandria Scrap Corp.*, *supra*, which rejected a Commerce Clause challenge to a Maryland statute offering a state bounty on inoperable automobile hulks which had the effect of disadvantaging *all* out-of-state scrap processors in relation to in-state processors. The case was decided on the ground that the state was acting as a market participant, but Justice Powell observed in dicta in his majority opinion, in language highly applicable to the Ohio ethanol tax incentive,

> that the commerce affected by the 1974 amendment appears to have been created, in whole or in substantial part, by the Maryland bounty scheme. We would hesitate to hold that the Commerce Clause forbids

7 Another contrast between Ohio Rev. Code § 5735.145(B) and the statutes in *A & P* and *Sporhase* is that the Ohio statute does not absolutely ban the sale of out-of-state ethanol; it merely denies a partial tax credit to the retailers who purchase such ethanol.



> state action reducing or eliminating a flow of commerce dependent for its existence upon state subsidy instead of private market forces.

426 U.S. at 809 n.18.

Justice Stevens' concurring opinion in *Hughes* explained this elemental concept more fully:

> It is important to differentiate between commerce which flourishes in a free market and commerce which owes its existence to a state subsidy program. Our cases finding that a state regulation constitutes an impermissible burden on interstate commerce all dealt with restrictions that adversely affected the operation of a free market. This case is unique because the commerce which Maryland has "burdened" is commerce which would not exist if Maryland had not decided to subsidize a portion of the automobile scrap-processing business.

*Id.* at 815;[8] *see also* Regan, *The Supreme Court and State Protectionism: Making Sense of the Dormant Commerce Clause*, 84 Mich. L. Rev. 1091, 1196 nn. 202, 203 (1986).

Viewed in this way, Ohio Rev. Code § 5735.145(B) does not impose any burden on interstate commerce. Ohio has created a tax incentive — applicable to both in-state and out-of-state ethanol — to encourage the production and use of ethanol. By so doing, it has given rise to commerce that "would not exist" without the incentive. Just as Ohio could not be criticized under the Commerce Clause for failing to create that commerce in the first instance, *Hughes*, 426 U.S. at 815-816 (Stevens, J., concurring), the State cannot be said to have burdened commerce by experimenting with a limit on the availability of its tax incentive in order to induce other states to create similar incentives. *Id.* at 817.

8 Justice Stevens noted that the result would not differ had the market been merely small rather than nonexistent before the bounty scheme was enacted: "the analysis is the same whether we are dealing with the newly created portion of a pre-existing market or with an entirely new market." *Id.*

The Commerce Clause limits the power of states "to erect barriers against interstate trade." *Lewis v. BT Investment Managers, Inc.*, 447 U.S. 27, 35 (1980); *see also Hughes*, 426 U.S. at 807. Allowing the states to encourage the development and expansion of a national market for an admittedly beneficial product that would otherwise have no market serves the very same interests in maintaining interstate trade that the Commerce Clause was meant to protect. Ohio Rev. Code § 5735.145(B) does not violate the Commerce Clause. On the contrary, it was enacted for a legitimate state purpose that is entirely consistent with those constitutional protections.

II. Ohio Rev. Code § 5735.145(B) Does Not Protect Local Producers At The Expense Of Interstate Commerce.

The Ohio Supreme Court correctly focused on the ultimate issue in this case: whether the statute had as its purpose economic protectionism. This Court has consistently prohibited states from favoring local producers at the expense of interstate commerce. *See, e.g., Bacchus Imports, Ltd. v. Dias*, 468 U.S. 263 (1984); *Hunt v. Washington State Apple Advertising Commission*, 432 U.S. 333 (1977); *see generally* Regan, *supra*. As the Supreme Court of Ohio properly found, however, Ohio Rev. Code § 5735.145(B) is not protectionist in either its purpose or effect. *New Energy Co. v. Limbach*, 32 Ohio St. 3d 206, 207 (1987), New Energy App. 4a.

If the Ohio legislature had wanted to protect Ohio ethanol producers such as South Point, Ohio Rev. Code § 5735.145(B) was a highly impractical means to achieve that purpose. A more effective means would have been to directly subsidize in-state producers, as did Indiana. Ohio instead enacted a tax credit that applies not only to in-state producers but also to producers from numerous other states, including Illinois, home of the nation's largest ethanol producer. The Ohio legislation did not insulate Ohio producers from competition with interstate competitors from these states. On the contrary, the statute has encouraged out-of-state producers from such states to participate in the Ohio market.



The presence of this vigorous interstate competition for Ohio business contrasts sharply with the situation in the cases cited by New Energy. For its argument that discriminatory laws impermissibly burden interstate commerce, New Energy principally relies upon *Boston Stock Exchange v. State Tax Commission*, 429 U.S. 318 (1977); *Bacchus Imports, supra; Armco, Inc. v. Hardesty*, 467 U.S. 638 (1984): and *Westinghouse Electric Corp. v. Tully*, 466 U.S. 388 (1984). In each of these cases, the statute at issue treated all out-of-state competitors differently from local competitors with the result that the "home team" received economic advantages unavailable to any outsider.

For example, in *Boston Stock Exchange* the state imposed a tax on all out-of-state stock transfers but not on in-state transactions. As a result, in-state stock exchanges were totally insulated from competition by out-of-state firms. This complete protection from out-of-state competition was the determinative factor in the Court's decision:

> [T]he fundamental principle that we find dispositive of the case now before us [is]:
>
> No State may, consistent with the Commerce Clause, "impose a tax which discriminates against interstate commerce . . . by providing a direct commercial advantage to local business."

*Boston Stock Exchange*, 429 U.S. at 329.

This dispositive factor of protectionism is totally absent from the present case.[9] Ohio Rev. Code § 5735.145(B) does not treat the interstate market differently from the intrastate market. As a result, the "home team" receives no advantage at the expense of all "outsiders." There is simply no discrimination against interstate commerce for the protection of a domestic producer.

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9 The same distinction can be drawn with the other cases relied upon by New Energy. *See, e.g., Bacchus Imports*, 468 U.S. at 271-272; *Armco*, 467 U.S. at 642; *Westinghouse*, 466 U.S. at 398.

The facts adduced at trial clearly showed that all interstate competitors in the Ohio market, except New Energy, received the Ohio credit. Finding 17, South Point App. 5a. Further, it is undisputed that these interstate competitors were ready, willing and able to supply New Energy's portion of the Ohio ethanol market, if New Energy removed itself from this market. *Id.* New Energy cannot escape the total absence of proof of discrimination against interstate commerce by simply asserting that such discrimination exists. The courts below properly concluded that Ohio Rev. Code § 5735.145(B) does not discriminate against interstate commerce and does not represent the type of economic protectionism that violates the Commerce Clause.

## III. New Energy Failed To Prove At Trial That The Statute Imposes A Burden On Interstate Commerce.

At every level of appeal of this case, New Energy has been unable to surmount the barrier of its failure to prove — or even to present any evidence — at trial that the Ohio statute imposes a burden on interstate commerce. Instead, New Energy merely asserts that the reciprocity provision "discriminates" against interstate commerce, and asks this Court to declare the statute unconstitutional without any supporting evidence. In fact, New Energy purposely created a situation where the courts could only speculate as to the existence of any burden that might result from the statute, by seeking trial on an expedited basis rather than waiting to see what the actual impact of the statute would be. New Energy then asked the courts to ignore long-established principles of constitutional decision-making and declare that the statute unconstitutionally burdens interstate commerce based purely upon speculation, rather than evidence.

This Court has traditionally applied two separate tests for measuring the states' compliance with the Commerce Clause:

> where simple economic protectionism is effected by state legislation, a virtually per se rule of invalidity has been erected.
>
> * * * *
>
> But where other legislative objectives are credibly advanced and there is no patent discrimination against interstate trade, the Court has adopted a much more flexible approach, the general contours of which were outlined in *Pike v. Bruce Church, Inc.*



*Philadelphia v. New Jersey,* 437 U.S. 617, 624 (1978). Because the Ohio statute benefits numerous out-of-state producers to the same extent that it benefits Ohio producers, the Supreme Court of Ohio properly refused to use the per se standard of review. *See A & P,* 424 U.S. at 371-372. In other cases involving reciprocity statutes, this Court has rejected the per se standard of review and instead applied the balancing test first articulated in *Pike v. Bruce Church, Inc.,* 397 U.S. 137, 142 (1970): when the statute "effectuate[s] a legitimate local public interest, and its effects on interstate commerce are only incidental, it will be upheld unless the burden imposed on such commerce is clearly excessive in relation to the putative local benefits." *See A & P,* 424 U.S. at 371-372. The party challenging a statute under the Commerce Clause has the burden of establishing that the statute imposes a burden on interstate commerce. *See, e.g., Exxon Corp. v. Governor of Maryland,* 437 U.S. 117, *reh'g denied sub nom. Shell Oil Co. v. Governor of Maryland,* 439 U.S. 884 (1978).

To warrant invalidation of Ohio Rev. Code § 5735.145(B) under the Commerce Clause, then, New Energy has the burden to prove — not hypothetically, but with substantive evidence — that (1) the provision imposes a burden on interstate commerce, and (2) the burden imposed clearly outweighs any legitimate state interest advanced in support of the statute. The record below and the findings of the trial court establish that New Energy failed to meet its burden of proof on these issues.[10]

This Court has rejected the premise "that every action by a State that has the effect of reducing in some manner the flow of

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10 Because New Energy failed to offer *any* evidence of a burden on interstate commerce, this Court need not analyze the extent of any such burden in relation to the purposes supporting the statute. *See Pike,* 397 U.S. at 142.

goods in interstate commerce" constitutes an impermissible burden under the Commerce Clause. *Hughes* 426 U.S. at 805. Because the Ohio ethanol tax incentive actually creates a market in interstate commerce for a product that would not otherwise be traded, it is inapposite to even characterize the statute as imposing a "burden" upon commerce at all. *Id.* In such circumstances, where the state has no obligation to create the market and certainly none to subsidize out-of-state businesses, "[w]hether the encouragement takes the form of a cash subsidy, a tax credit or a special privilege intended to attract investment capital, it should not be characterized as a 'burden' on commerce." *Id.* at 816 (Stevens, J., concurring). Even where the incentive is not available to all out-of-state potential market participants, the "burden" caused by nonreceipt of the benefit is not the type of burden that implicates the Commerce Clause. *Id.* at 816-817.

Even if Ohio Rev. Code § 5735.145(B) could be characterized in the abstract as creating a burden on the interstate market, New Energy has failed to prove the existence of any such burden. Instead, New Energy has focused only on the potential impact of the statute on New Energy's own business. This Court has stated, however, that "[t]he fact that the burden of a state regulation falls on some interstate companies does not, by itself, establish a claim of discrimination against interstate commerce." *Exxon*, 437 U.S. at 126; *see also CTS Corp. v. Dynamic Corp. of America*, 107 S. Ct. 1637, 1649 (1987). The challenged statute in *Exxon* prohibited a producer or refiner of petroleum products from operating any retail service station within the state of Maryland. The plaintiff in *Exxon* complained that the statute would require it to stop selling its product in Maryland. The Court concluded, however, that the plaintiff's withdrawal from the market would not warrant:

> . . . a finding that the statute impermissibly burdened interstate commerce. Some refiners may choose to withdraw entirely from the Maryland market, but there is no reason to assume that their share of the entire supply will not be promptly replaced by other interstate refiners. The source of the consumers' supply may switch from company-operated stations to independent dealers, but interstate commerce is not subjected to an impermissible burden simply because an otherwise valid regulation causes some business to shift from one interstate supplier to another.



*Exxon*, 437 U.S. at 126-127. In other words, the Commerce Clause is concerned with the impact of a statute on the total flow of interstate commerce from all sources rather than the potential impact upon a single company. *Id.* at 126 n.16; *Minnesota v. Clover Leaf Creamery Co.*, 449 U.S. 456, 474, *reh'g denied* 450 U.S. 1027 (1981).

This analysis of the Commerce Clause does not mean that a state may arbitrarily discriminate against a particular business. Rather, it recognizes that the protection of specific firms stems from the Equal Protection Clause, not the Commerce Clause. As this Court recently explained: "The two constitutional provisions perform different functions in the analysis of the permissible scope of a State's power — one protects interstate commerce, and the other protects persons from unconstitutional discrimination by the States." *Ward*, 470 U.S. at 881 (footnote omitted).

New Energy initially brought its claim under the Equal Protection Clause as well as the Commerce Clause. After this Court announced its decision in *Ward*, however, New Energy withdrew its Equal Protection claim. New Energy now attempts to base its Commerce Clause claim on proof that, at best, goes to the Equal Protection question rather than the issue of a burden upon interstate commerce taken as a whole.

The only evidence in the record regarding the impact of the statute related to its potential effect on New Energy. There was no evidence of any burden on any other out-of-state producer of

ethanol or on the general flow of ethanol into Ohio from outside the state. A minimum of three out-of-state producers sell ethanol in Ohio, and have adequate capacity to replace the share of the market served by New Energy. Finding 17, South Point App. 5a. Thus, the purported "competitive disadvantage" of which New Energy complains is not limited to a comparison with merely local producers, but includes several interstate competitors as well.

New Energy has not proved that the Ohio statute imposes *any* burden on interstate commerce, let alone a "clearly excessive" burden. *See Pike*, 397 U.S. at 142. The lower courts correctly applied the constitutional test mandated by this Court and held, as a result, that New Energy had failed to establish its claim challenging the constitutionality of Ohio Revised Code § 5735.145(B).

## CONCLUSION

The Courts below properly held that Ohio Revised Code Section 5735.145(B) was not enacted for purposes of economic protectionism, that the Ohio legislature had a legitimate purpose for enacting the statute and that New Energy failed to prove that the statute imposed a burden upon interstate commerce. For the foregoing reasons, the Court should affirm the judgment of the Supreme Court of Ohio or, in the alternative, this appeal should be dismissed.

Respectfully submitted,

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November 20, 1987

# APPENDIX

IN THE COURT OF COMMON PLEAS,
FRANKLIN COUNTY, OHIO

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|---|---|---|
| NEW ENERGY COMPANY OF INDIANA, *Plaintiff,* | : | Case No. 85CV-02-712 |
| v. | : | Judge Crawford |
| JOANNE LIMBACH TAX COMMISSIONERS, *et al.,* *Defendants.* | : | |

## AMENDED AGREED FINDINGS OF FACT

The parties agree that the record in this case supports these Agreed Findings of Fact. This agreement does not waive any objection by any party as to the relevancy of any agreed fact nor does it limit any party from proposing any additional findings of fact.

1. The plaintiff, New Energy Company of Indiana ("New Energy"), is an Indiana limited partnership engaged in Commerce among the states in the business of manufacturing ethanol. The plaintiff's manufacturing facility is located in South Bend, Indiana (Tr. 5). The plaintiff is the only ethanol manufacturer with production facilities in Indiana. Ethanol produced by New Energy is presently sold to blenders in several states including Ohio, Indiana and Illinois. (Plaintiff's Exs. 1 and 2)

2. New Energy was formed in 1980 and fully capitalized in 1982 by a public offering. The equity capital invested in the entity is $40,000,000 and the equity investors guaranteed an additional $20,000,000 in loans to the partnership (Tr. 5).

3. The total project cost of the New Energy facility was in excess of $185,000,000. Approximately $150,000,000 of the project cost was funded by bank loans, the principal of which is



90% guaranteed by the United States Department of Energy pursuant to the Energy Security Act of 1980. The United States Department of Energy has also made a direct loan to New Energy in the amount of $1,769,000 (Tr. 7).

4. The state defendants are Joanne Limbach, Tax Commissioner of the State of Ohio, and Mary Ellen Withrow, Treasurer of the State of Ohio. Together these defendants are charged with the responsibility of administering and enforcing R.C. Chapter 5735 dealing with motor vehicle fuel taxes.

5. South Point Ethanol ("South Point") intervened in this action as a defendant on March 27, 1985. South Point is a joint venture between Ashland Oil Company, the Ohio Farm Bureau, UGI and Publicker Industries which produces ethanol in Lawrence County, Ohio.

6. South Point was formed in 1981 to retrofit a closed chemical plant. Its facility is located in South Point, Ohio. The joint venturers have invested approximately $120,000,000 in South Point. Additionally, South Point provides approximately 185 jobs and expends $100,000,000 annually in the production of ethanol from corn.

7. The plaintiff's complaint seeks a declaration that Ohio R.C. § 5735.145(B), as amended, is unconstitutional as being violative of the United States and Ohio Constitutions. The complaint further seeks a preliminary and permanent injunction against defendants from implementing and enforcing the allegedly unconstitutional provisions.

8. Defendants answered the complaint and raised the affirmative defenses of failure to state a claim upon which relief can be granted, lack of jurisdiction over the subject matter, lack of standing to maintain the action and failure to comply with statutory requirements for commencing an action. In addition, the defendants allege that R.C. § 5703.38 prohibits the Court from granting the injunctive relief demanded by plaintiff and that plaintiff lacks standing to sue with respect to injunctive relief sought under R.C. § 2723.01.

9. Ethanol is a 199 proof alcohol. It is derived from corn which is treated with enzymes that convert the starch to sugar and ultimately into alcohol. Ethanol is mixed with gasoline in a 10/90% ratio to form a blend commonly referred to as gasohol (Tr. 14).

10. Ethanol is beneficial as a fuel additive to increase the octane rating of gasoline without contributing any additional lead into the environment. Ethanol is, in fact, the cost effective replacement for lead in gasoline and is the most environmentally benign replacement for lead. The production of ethanol also provides an outlet for the sale of corn surpluses (Tr. 9).

11. Various governmental bodies have initiated programs to encourage the production of ethanol. The United States Department of Energy provides grants for feasibility studies and guarantees 90% of certain qualifying loans (Tr. 9). To encourage the use of ethanol, the Department of Treasury exempts ethanol/gasoline blends from 6¢ of the 9¢ federal excise tax on gasoline (Tr. 9). In addition, at least thirty-two states allow credits from their respective motor fuel taxes for ethanol/gasoline blends (Tr. 10). The provision of tax credits has been the best method adopted by the Federal and state government to encourage the use of ethanol.

12. Ohio imposes a tax on dealers for each gallon of gasoline sold in Ohio. This tax is not imposed on, paid by, or collected by New Energy, South Point or any other producer of ethanol. Prior to January 1, 1985, Ohio law provided a tax credit of 35 cents per gallon for each gallon of ethanol blended with gasoline in not more than a 10% ratio and used, sold, or distributed by dealers in Ohio. This credit was available to dealers on all ethanol blends used, sold, or distributed in Ohio, regardless of where the ethanol ingredients of such blends were made (Tr. 19). (Plaintiff's Exs. 5 and 6).

13. Ohio's tax treatment of ethanol containing products was altered by the enactment of R.C. § 5735.145(B) which limits the availability of the credit to Ohio produced ethanol and ethanol produced in states which grant similar credits to



ethanol produced in Ohio and sold within that state (Tr. 23). The newly enacted R.C. § 5735.145(B) provides that:

> The qualified fuel otherwise eligible for the qualified fuel credit shall not contain ethanol produced outside Ohio unless the Tax Commissioner determines that the fuel claimed to be eligible for credit contains ethanol produced in a state that also grants an exemption, credit or refund from such state's motor vehicle fuel excise tax or sales tax for similar fuel containing ethanol produced in Ohio; provided however, that such credit shall not exceed the amount of the credit allowable for qualified fuel containing ethanol produced in Ohio.

Prior to the adoption of R.C. § 5735.145(B) representatives of South Point testified before the House Ways and Means Committee of the Ohio General Assembly regarding all of the benefits of the use of ethanol, including, among other things, the public health benefits of its use as a substitute for lead as an octane enhancement in gasoline.

14. But for the enactment and operation of R.C. § 5735.145(B) plaintiff would receive identical tax treatment by the Ohio authorities as that accorded to any other Ohio dealer or producer of ethanol. The validity or invalidity of subsection (B) does not affect any other provision of or the application of R.C. §5735.145.

15. The tax credit provided for in R.C. § 5735.145(B) has been applied in the manner provided by R.C. Chapter 5735 on the ethanol sold by plaintiff in Ohio during January and February of 1985 (Tr. 25). (Plaintiff's Exs. 3 and 4).

16. The impact of the application of R.C. § 5735.145 is being felt by the plaintiff on a graduated basis during the period of January 1, 1985 through July 1, 1985. Dealers of gasohol containing ethanol produced by the plaintiff received the full 25¢ a gallon credit available to retailers on spot sales in Ohio during January and February of 1985 (Tr. 19). Prior to January 1, 1985 the credit available to dealers of gasohol containing ethanol was 35¢ per gallon (Tr. 19). The credit applicable to

dealers of gasohol containing ethanol produced by the plaintiff is recalculated monthly by the Ohio Department of Taxation (Tr. 24). During the month of March the credit was 24¢ per gallon. By July 1, 1985 R.C. § 5735.145(B) is fully applicable to all sales of ethanol by the plaintiff including both spot sales and contract sales (Tr. 23-24). After July 1, 1985 Ohio dealers of gasohol containing ethanol produced by the plaintiff will not receive any credit while retailers selling gasohol blended with non-Indiana ethanol will continue to receive 25¢ per gallon credit (Tr. 23). (Plaintiff's Exs. 7).

17. New Energy and South Point compete for the sale of ethanol to Ohio dealers with Archer Daniels Midland ("ADM"), Pekin Energy ("Pekin") and A.E. Staley ("Staley"). ADM and Pekin have production facilities in Illinois; Staley had production facilities in Tennessee. Ethanol produced in these facilities is entitled to the full Ohio credit. Additionally, ADM, Pekin and Staley have the capacity to supply the portion of the Ohio market for ethanol presently being filled by the plaintiff.

18. The evidence showed that the decreased credits afforded to retailers of blended gasoline containing plaintiff's product for January and February of 1985 decreased the price paid to plaintiff for its product (Tr. 27). (Plaintiff's Ex. 6) The decreased credits will continue to affect the price paid to plaintiff for its product through July 1, 1985. After July 1, 1985, the plaintiff believes that the application of R.C. § 5735.145(B) will affect the price paid to plaintiff for its product to the extent that the plaintiff will be unable to sell its ethanol in Ohio (Tr. 23).

19. The amount of state tax credit available to dealers of ethanol on a gallon of ethanol directly affects the per gallon price that dealers pay to ethanol producers in that the lower the available credit, the lower the price paid to ethanol producers for a gallon of ethanol (Tr. 28-29).

20. The continued enforcement of R.C. § 5735.145(B) will cause financial hardship to plaintiff.

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IN THE COURT OF COMMON PLEAS,
FRANKLIN COUNTY, OHIO

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| NEW ENERGY COMPANY OF INDIANA, *Plaintiff*, | Case No. 85CV-02-712 |
| v. | Judge Crawford |
| JOANNE LIMBACH, TAX COMMISSIONER, *et al.*, *Defendants*. | |

**PROPOSED ADDITIONAL FINDINGS OF FACT AND CONCLUSIONS OF LAW OF DEFENDANTS JOANNE LIMBACH, TAX COMMISSIONER OF OHIO, AND MARY ELLEN WITHROW, TREASURER OF OHIO**

1. It is conceivable that the Ohio General Assembly may have had several purposes in enacting R. C. § 5735.145(B), none of which were explicitly declared in the enactment itself. One of these purposes was to provide a cleaner and safer environment for Ohio citizens by encouraging the use of ethanol as a replacement for lead in gasoline not only in Ohio but in all states.

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IN THE COURT OF COMMON PLEAS,
FRANKLIN COUNTY, OHIO

| | | |
|---|---|---|
| NEW ENERGY COMPANY OF INDIANA, *Plaintiff*, | : | Case No. 85CV-02-712 |
| v. | : | Judge Crawford |
| JOANNE LIMBACH, TAX COMMISSIONER, *et al.*, *Defendants*. | : | |

**NEW ENERGY COMPANY OF INDIANA'S POST-TRIAL ADDITIONAL PROPOSED FINDINGS OF FACT AND CONCLUSIONS OF LAW**

Pursuant to the Court's instructions, the parties filed Agreed Findings of Fact. The plaintiff submits the following additional findings of fact which are supported by the record for review and inclusion into the Court's findings but to which the parties could not agree. The new language in prior findings is underlined.

**ADDITIONAL PROPOSED FINDINGS OF FACT**

11. Various governmental bodies have initiated programs to encourage the *production and use* of ethanol (Tr. #1, at 9). The United States Department of Energy provides loan guarantees and feasibility study grants to develop the technology to *produce* ethanol more efficiently (Tr. #1, at 9). To encourage the *production and use* of ethanol, the Department of Treasury exempts ethanol/gasoline blends from 6¢ of the 9¢ federal excise tax on gasoline (Tr. #1, at 9-10). In addition, at least 32 states encourage the *production and use* of ethanol by allowing a credit from their respective motor fuel taxes for ethanol/gasoline blends (Tr. #1, at 10). The provision of tax credits has been the best method adopted by the federal and state governments to encourage the *production and use* of ethanol.



20. The continued enforcement of R.C. § 5735.145(B) will cause *severe* financial hardship to plaintiff and threaten plaintiff's continued viability (Tr. #1, at 44).

21. Representatives of South Point lobbied the Ohio General Assembly to enact the reciprocity provision provided for in R.C. § 5735.145(B) for the stated purpose of providing an incentive to other states to pass similar legislation (Tr. #2, at 57 and 60).

22. Intervenor raised the issue of necessary filings with the Secretary of State by the plaintiff and New Energy Corporation of Indiana, the general partner of the plaintiff. Although Ohio R.C. §1782.49 was not effective until at least April 1, 1985, if after a review of the legal authorities cited by intervenor, plaintiff believes that the subsequent filings made by it are relevant, additional findings of fact concerning these filings (of which the Court may take judicial notice), will be presented along with the Reply Brief.

* * * *

## CERTIFICATE OF SERVICE

The undersigned hereby certifies that copies of the foregoing have been served by regular United States mail, first-class, postage prepaid, upon David J. Young, Esq., Murphey, Young & Smith, 250 East Broad Street, Columbus, Ohio 43215 and Herman Schwartz, Esq., 207 Myers Hall, 4400 Massachusetts Avenue, N.W., Washington, D.C. 20016, counsel for Appellant; and Richard C. Farrin, Esq., Assistant Attorney General, 30 East Broad Street, Columbus, Ohio 43215, counsel for Appellees Joanne Limbach and Mary Ellen Withrow and that all parties required to be served have been served on this 20th day of November, 1987.

DAVID C. CRAGO